PENTAIR INC
Form 10-Q
May 04, 2007

Table of Contents

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

þ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the Quarterly Period Ended March 31, 2007

OR

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

Commission file number 1-11625
Pentair, Inc.
(Exact name of Registrant as specified in its charter)

Minnesota	**41-0907434**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification number)**
5500 Wayzata Blvd, Suite 800, Golden Valley, Minnesota	**55416**
(Address of principal executive offices)	**(Zip code)**

Registrant s telephone number, including area code: (763) 545-1730

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days. Yes þ No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer (as defined in Rule 12b-2 of the Act). Large accelerated filer þ Accelerated filer o Non-accelerated filer o

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No þ

On April 27, 2007, 99,789,104 shares of the Registrant s common stock were outstanding.

Pentair, Inc. and Subsidiaries

Table of Contents

PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

Pentair, Inc. and Subsidiaries
Condensed Consolidated Statements of Income (Unaudited)

	Three months ended	
In thousands, except per-share data	**March 31 2007**	**April 1 2006**
Net sales	$807,995	$771,389
Cost of goods sold	570,592	548,881
Gross profit	237,403	222,508
Selling, general and administrative	142,300	129,089
Research and development	14,950	14,863
Operating income	80,153	78,556
Net interest expense	15,120	13,284
Income from continuing operations before income taxes	65,033	65,272
Provision for income taxes	22,903	22,201
Income from continuing operations	42,130	43,071
Gain (loss) on disposal of discontinued operations, net of tax	143	(1,451)
Net income	$ 42,273	$ 41,620
Earnings (loss) per common share		
Basic		
Continuing operations	$ 0.43	$ 0.43
Discontinued operations		(0.01)
Basic earnings per common share	$ 0.43	$ 0.42
Diluted		
Continuing operations	$ 0.42	$ 0.42
Discontinued operations		(0.01)
Diluted earnings per common share	$ 0.42	$ 0.41
Weighted average common shares outstanding		
Basic	98,966	100,493
Diluted	100,271	102,492
Cash dividends declared per common share	$ 0.15	$ 0.14

See accompanying notes to condensed consolidated financial statements.

3

Table of Contents

Pentair, Inc. and Subsidiaries
Condensed Consolidated Balance Sheets (Unaudited)

In thousands, except share and per-share data	March 31 2007	December 31 2006	April 1 2006
Assets			
Current assets			
Cash and cash equivalents	$ 64,230	$ 54,820	$ 50,237
Accounts and notes receivable, net	532,792	422,134	520,968
Inventories	413,178	398,857	375,619
Deferred tax assets	52,198	50,578	44,432
Prepaid expenses and other current assets	41,907	31,239	28,921
Total current assets	1,104,305	957,628	1,020,177
Property, plant and equipment, net	351,211	330,372	314,164
Other assets			
Goodwill	1,830,359	1,718,771	1,723,952
Intangibles, net	384,933	287,011	262,829
Other	69,505	71,197	67,561
Total other assets	2,284,797	2,076,979	2,054,342
Total assets	$3,740,313	$3,364,979	$3,388,683
Liabilities and Shareholders Equity			
Current liabilities			
Short-term borrowings	$ 16,003	$ 14,563	$
Current maturities of long-term debt	8,257	7,625	4,246
Accounts payable	208,713	206,286	206,528
Employee compensation and benefits	85,741	88,882	75,536
Current pension and post-retirement benefits	7,918	7,918	
Accrued product claims and warranties	42,766	44,093	42,238
Income taxes	13,525	22,493	27,195
Accrued rebates and sales incentives	31,293	39,419	23,353
Other current liabilities	91,402	90,003	94,418
Total current liabilities	505,618	521,282	473,514
Other liabilities			
Long-term debt	1,056,495	721,873	888,015
Pension and other retirement compensation	213,512	207,676	158,535
Post-retirement medical and other benefits	47,401	47,842	73,812
Long-term income taxes payable	14,412		
Deferred tax liabilities	111,106	109,781	123,663
Other non-current liabilities	85,912	86,526	76,452

Total liabilities	2,034,456	1,694,980	1,793,991
Commitments and contingencies			
Shareholders equity			
Common shares par value $0.16 $^{2/3}$; 99,777,660, 99,777,165 and 101,642,814 shares issued and outstanding, respectively	16,629	16,629	16,940
Additional paid-in capital	484,376	488,540	524,904
Retained earnings	1,172,459	1,148,126	1,048,374
Accumulated other comprehensive income	32,393	16,704	4,474
Total shareholders equity	1,705,857	1,669,999	1,594,692
Total liabilities and shareholders equity	$3,740,313	$3,364,979	$3,388,683

See accompanying notes to condensed consolidated financial statements.

Table of Contents

Pentair, Inc. and Subsidiaries
Condensed Consolidated Statements of Cash Flows (Unaudited)

In thousands	Three months ended March 31 2007	April 1 2006
Operating activities		
Net income	$ 42,273	$ 41,620
Adjustments to reconcile net income to net cash used for operating activities		
(Gain) loss on disposal of discontinued operations	(143)	1,451
Depreciation	15,523	15,230
Amortization	4,900	4,258
Deferred income taxes	(355)	2,483
Stock compensation	6,218	6,646
Excess tax benefits from stock-based compensation	(1,063)	(2,532)
Changes in assets and liabilities, net of effects of business acquisitions and dispositions		
Accounts and notes receivable	(99,387)	(95,541)
Inventories	(6,381)	(25,379)
Prepaid expenses and other current assets	(8,770)	(4,258)
Accounts payable	7,886	(4,041)
Employee compensation and benefits	(13,081)	(23,528)
Accrued product claims and warranties	(1,403)	(1,363)
Income taxes	(1,448)	10,717
Other current liabilities	(7,638)	(26,140)
Pension and post-retirement benefits	4,033	4,477
Other assets and liabilities	1,167	3,550
Net cash used for continuing operations	(57,669)	(92,350)
Net cash provided by operating activities of discontinued operations		48
Net cash used for operating activities	(57,669)	(92,302)
Investing activities		
Capital expenditures	(18,865)	(9,054)
Proceeds from sale of property and equipment	1,329	79
Acquisitions, net of cash acquired	(230,581)	(2,158)
Divestitures		(24,007)
Other		(2,150)
Net cash used for investing activities	(248,117)	(37,290)
Financing activities		
Net short-term borrowings	1,234	
Proceeds from long-term debt	345,190	272,906
Repayment of long-term debt	(10,250)	(133,051)
Proceeds from exercise of stock options	1,762	2,577

Repurchases of common stock	(9,280)	
Excess tax benefits from stock-based compensation	1,063	2,532
Dividends paid	(15,022)	(14,224)
Net cash provided by financing activities	314,697	130,740
Effect of exchange rate changes on cash and cash equivalents	499	589
Change in cash and cash equivalents	9,410	1,737
Cash and cash equivalents, beginning of period	54,820	48,500
Cash and cash equivalents, end of period	$ 64,230	$ 50,237

See accompanying notes to condensed consolidated financial statements.

Pentair, Inc. and subsidiaries
Notes to condensed consolidated financial statements (unaudited)

1. Basis of Presentation and Responsibility for Interim Financial Statements

We prepared the unaudited condensed consolidated financial statements following the requirements of the Securities and Exchange Commission (SEC) for interim reporting. As permitted under those rules, certain footnotes or other financial information that are normally required by accounting principles generally accepted in the United States can be condensed or omitted.

We are responsible for the unaudited financial statements included in this document. The financial statements include all normal recurring adjustments that are considered necessary for the fair presentation of our financial position and operating results. As these are condensed financial statements, one should also read our consolidated financial statements and notes thereto, which are included in our 2006 Annual Report on Form 10-K for the year ended December 31, 2006.

Revenues, expenses, cash flows, assets and liabilities can and do vary during each quarter of the year. Therefore, the results and trends in these interim financial statements may not be indicative of those for a full year.

Our fiscal year ends on December 31. We report our interim quarterly periods on a 13-week basis ending on a Saturday.

2. New Accounting Standards

In June 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48 *Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement 109* (FIN 48). FIN 48 prescribes a comprehensive model for recognizing, measuring, presenting and disclosing in the financial statements tax positions taken or expected to be taken on a tax return, including a decision whether to file or not to file a tax return in a particular jurisdiction. FIN 48 is effective for fiscal years beginning after December 15, 2006 and we adopted it on January 1, 2007. The adoption of FIN 48 increased total liabilities by $2.9 million and decreased total shareholders equity by $2.9 million. The adoption of FIN 48 had no impact on our consolidated results of operations.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements* (SFAS 157). SFAS 157 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. SFAS 157 does not require any new fair value measurements, but rather eliminates inconsistencies in guidance found in various prior accounting pronouncements. SFAS 157 is effective for fiscal years beginning after November 15, 2007. We are currently evaluating the impact of adopting SFAS 157 on our consolidated results of operations and financial condition.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* (SFAS 159). SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value. SFAS 159 is effective for fiscal years beginning after November 15, 2007. We are currently evaluating the impact of adopting SFAS 159 on our consolidated results of operations and financial condition.

In March 2007, the FASB ratified the Emerging Issues Task Force (EITF) Issue No. 06-11, *Accounting for Income Tax Benefits of Dividends on Share Based Payment Awards* (EITF 06-11). EITF 06-11 requires companies to recognize the income tax benefit realized from dividends or dividend equivalents that are charged to retained earnings and paid to employees for nonvested equity-classified employee share-based awards as an increase to additional paid-in capital. EITF 06-11 is effective for fiscal years beginning after September 15, 2007. We are currently evaluating the impact of adopting EITF 06-11 on our consolidated results of operations and financial condition.

3. Stock-based Compensation

Total stock-based compensation expense for the first quarter of 2007 and 2006 was $6.2 million and $6.6 million, respectively.

Non-vested shares of our common stock were granted during the first quarter of 2007 and 2006 to eligible employees with a vesting period of two to five years after issuance. Non-vested share awards are valued at market value on the date of grant and are typically expensed over the vesting period. Total compensation expense for non-vested share awards during the first quarter of 2007 and 2006 was $2.8 million and $2.3 million, respectively.

During the first quarter of 2007, option awards were granted under the Omnibus Stock Incentive Plan and the Outside Directors Nonqualified Stock Option Plan (together the Plans), each with an exercise price equal to the market price of our common stock on the date of grant. Prior to 2006, option grants under the Plans typically had a reload feature when shares were retired to pay the exercise price, allowing individuals to receive additional options upon exercise equal to the number of shares retired. Option awards granted after 2005 under the Plans do not have a reload feature attached to the option. The options vest one-third each year over a three-year period and have a ten-year contractual term. Compensation expense equal to the grant date fair value is recognized for these awards typically over the vesting period. No option grants were reloaded during the quarter for individuals retiring shares to pay the exercise price of options granted prior to 2006. Reload options are vested and expensed immediately. Total compensation expense for stock option awards was $3.4 and $4.3 million for the first quarter of 2007 and 2006, respectively.

Table of Contents

Pentair, Inc. and subsidiaries
Notes to condensed consolidated financial statements (unaudited)

We estimated the fair value of each stock option award on the date of grant using a Black-Scholes option pricing model, modified for dividends and using the following assumptions:

	March 31 2007	**April 1 2006**
Expected stock price volatility	28.5%	31.5%
Expected life	4.8 yrs.	4.5 yrs.
Risk-free interest rate	4.66%	4.56%
Dividend yield	1.95%	1.44%

The weighted-average fair value of options granted during the first quarter of 2007 and 2006 was $8.29 and $11.49 per share, respectively.

These estimates require us to make assumptions based on historical results, observance of trends in our stock price, changes in option exercise behavior, future expectations, and other relevant factors. If other assumptions had been used, stock-based compensation expense, as calculated and recorded under SFAS No. 123R, could have been affected. We based the expected life assumption on historical experience as well as the terms and vesting periods of the options granted. For purposes of determining expected volatility, we considered a rolling-average of historical volatility measured over a period approximately equal to the expected option term. The risk-free rate for periods that coincide with the expected life of the options is based on the U.S. Treasury Department yield curve in effect at the time of grant.

4. Earnings Per Common Share

Basic and diluted earnings per share were calculated using the following:

	Three months ended	
In thousands, except per-share data	**March 31 2007**	**April 1 2006**
Earnings (loss) per common share basic		
Continuing operations	$ 42,130	$ 43,071
Discontinued operations	143	(1,451)
Net income	$ 42,273	$ 41,620
Continuing operations	$ 0.43	$ 0.43
Discontinued operations		(0.01)
Basic earnings per common share	$ 0.43	$ 0.42
Earnings (loss) per common share diluted		
Continuing operations	$ 42,130	$ 43,071
Discontinued operations	143	(1,451)
Net income	$ 42,273	$ 41,620

Continuing operations	$ 0.42	$ 0.42
Discontinued operations		(0.01)
Diluted earnings per common share	$ 0.42	$ 0.41
Weighted average common shares outstanding basic	98,966	100,493
Dilutive impact of stock options and restricted stock	1,305	1,999
Weighted average common shares outstanding diluted	100,271	102,492
Stock options excluded from the calculation of diluted earnings per share because the exercise price was greater than the average market price of the common shares	3,675	2,079

7

Pentair, Inc. and subsidiaries
Notes to condensed consolidated financial statements (unaudited)

5. Acquisitions

On April 30, 2007, we acquired as part of our Water Group all of the capital interests in Porous Media, a privately held filtration and separation technologies business, for $225.0 million, excluding transaction costs and subject to a post-closing net asset value adjustment. Porous Media s product portfolio includes high-performance filter media, membranes and related filtration products and purification systems for liquids, gases and solids for general industrial, petrochemical, refining and healthcare market segments among others. We announced the Porous Media acquisition on March 6, 2007.

On February 2, 2007, we acquired as part of our Water Group all the outstanding shares of capital stock of Jung Pumpen GmbH (Jung) for $230.2 million, including a cash payment of $239.9 million and transaction costs of $0.7 million, less cash acquired of $10.4 million. The purchase price is subject to a post-closing net asset value adjustment. Jung is a leading German manufacturer of wastewater products for municipal and residential markets. Jung brings us its strong application engineering expertise and a complementary product offering, including a new line of water re-use products, submersible wastewater and drainage pumps, wastewater disposal units and tanks. Jung also brings to Pentair its well-established European presence, a state-of-the-art training facility in Germany, and sales offices in Germany, Austria, France, Hungary, Poland and Slovakia. Goodwill recorded as part of the initial purchase price allocation was $103.2 million, of which approximately $53 million is tax deductible. We continue to evaluate the purchase price allocation for the Jung acquisition, including intangible assets, contingent liabilities, and property, plant and equipment. We expect to revise the purchase price allocation as better information becomes available.

On April 12, 2006, we acquired as part of our Water Group the assets of Geyer s Manufacturing & Design Inc. and FTA Filtration, Inc. (together Krystil Klear), two privately-held companies, for $15.5 million in cash. Krystil Klear expands our industrial filtration product offering to include a full range of steel and stainless steel tanks which house filtration solutions. Goodwill recorded as part of the purchase price allocation was $9.5 million, all of which is tax deductible.

During 2006, we completed several other small acquisitions totaling $14.2 million in cash and notes payable, adding to both our Water and Technical Products Groups. Total goodwill recorded as part of the initial purchase price allocations was $7.9 million, of which $2.9 million is tax deductible. We continue to evaluate the purchase price allocations for these acquisitions and expect to revise the purchase price allocations as better information becomes available.

The following pro forma condensed financial results of operations are presented as if the acquisitions described above (with the exception of Porous Media) had been completed at the beginning of each period.

	Three months ended	
In thousands, except per-share data	**March 31 2007**	**April 1 2006**
Pro forma net sales from continuing operations	$814,171	$795,334
Pro forma net income from continuing operations	42,403	43,933
Pro forma earnings per common share continuing operations		
Basic	$ 0.43	$ 0.44
Diluted	$ 0.42	$ 0.43
Weighted average common shares outstanding		
Basic	98,966	100,493
Diluted	100,271	102,492

These pro forma condensed consolidated financial results have been prepared for comparative purposes only and include certain adjustments, such as increased interest expense on acquisition debt. They do not reflect the effect of costs or synergies that would have been expected to result from the integration of these acquisitions. The pro forma information does not purport to be indicative of the results of operations that actually would have resulted had the combination occurred at the beginning of each period presented, or of future results of the consolidated entities.

6. Discontinued Operations

Effective after the close of business on October 2, 2004, we completed the sale of our former Tools Group to The Black & Decker Corporation (BDK). In January 2006, pursuant to the purchase agreement for the sale of our former Tools Group, we completed the repurchase of a manufacturing facility in Suzhou, China from BDK for approximately $5.7 million. We recorded no gain or loss on the repurchase. In March 2006, we completed an outstanding net asset value arbitration with BDK relating to the purchase price for the sale of our former Tools Group. The decision by the arbitrator constituted a final resolution of all disputes between BDK and us regarding the net asset value. We paid the final net asset value purchase price adjustment pursuant to the purchase agreement of $16.1 million plus interest of $1.1 million in March 2006, resulting in an incremental pre-tax loss on disposal of discontinued operations of $3.4 million or $1.6 million net of tax.

Table of Contents

Pentair, Inc. and subsidiaries
Notes to condensed consolidated financial statements (unaudited)

In 2001, we completed the sale of our former Service Equipment businesses (Century Mfg. Co./Lincoln Automotive Company) to Clore Automotive, LLC. In the fourth quarter of 2003, we reported an additional loss from discontinued operations of $2.9 million related to exiting the remaining two facilities. In March 2006, we exited a leased facility from our former Service Equipment business resulting in a net cash outflow of $2.2 million and an immaterial gain from disposition.

Operating results of the discontinued operations for the first quarter of 2007 and 2006 are summarized below:

In thousands	**Three months ended March 31 2007**	**Three months ended April 1 2006**
Gain (loss) on disposal of discontinued operations	$225	$(3,254)
Income tax (expense) benefit	(82)	1,803
Gain (loss) on disposal of discontinued operations, net of tax	$143	$(1,451)

7. Inventories

Inventories were comprised of:

In thousands	**March 31 2007**	**December 31 2006**	**April 1 2006**
Raw materials and supplies	$193,049	$186,508	$162,274
Work-in-process	56,978	55,141	49,590
Finished goods	163,151	157,208	163,755
Total inventories	$413,178	$398,857	$375,619

8. Comprehensive Income

Comprehensive income and its components, net of tax, were as follows:

In thousands	**Three months ended March 31 2007**	**Three months ended April 1 2006**
Net income	$42,273	$41,620
Changes in cumulative foreign currency translation adjustment	15,926	3,897
Changes in market value of derivative financial instruments classified as cash flow hedges	(237)	1,563
Comprehensive income	$57,962	$47,080

9. Goodwill and Other Intangible Assets

Changes in the carrying amount of goodwill for the three months ended March 31, 2007 by segment were as follows:

In thousands	**Water**	**Technical Products**	**Consolidated**

Balance at December 31, 2006	$1,449,460	$269,311	$1,718,771
Acquired	100,841		100,841
Purchase accounting adjustments	748	(198)	550
Foreign currency translation	5,584	4,613	10,197
Balance at March 31, 2007	$1,556,633	$273,726	$1,830,359

The acquired goodwill relates to the Jung acquisition. The purchase accounting adjustments recorded during the first quarter of 2007 related to the Krystil Klear acquisition and other small acquisitions. We finalized our purchase price allocation for the Krystil Klear acquisition during the first quarter of 2007.

Table of Contents

Pentair, Inc. and subsidiaries
Notes to condensed consolidated financial statements (unaudited)

Intangible assets, other than goodwill, were comprised of:

	March 31, 2007			**December 31, 2006**			**April 1, 2006**		
In thousands	**Gross carrying amount**	**Accum. amort**	**Net**	**Gross carrying amount**	**Accum. amort**	**Net**	**Gross carrying amount**	**Accum. amort**	**Net**
Finite-life intangibles									
Patents	$ 15,437	$ (6,475)	$ 8,962	$ 15,433	$ (6,001)	$ 9,432	$ 15,455	$ (4,589)	$ 10,866
Non-compete agreements	4,022	(3,031)	991	4,343	(3,091)	1,252	3,940	(2,276)	1,664
Proprietary technology	45,834	(9,056)	36,778	45,755	(8,240)	37,515	51,378	(6,195)	45,183
Customer relationships	157,992	(18,403)	139,589	110,616	(15,924)	94,692	87,525	(10,077)	77,448
Total finite-life intangibles	$ 223,285	$ (36,965)	$ 186,320	$ 176,147	$ (33,256)	$ 142,891	$ 158,298	$ (23,137)	$ 135,161
Indefinite-life intangibles									
Brand names	$ 198,613	$	$ 198,613	$ 144,120	$	$ 144,120	$ 127,668	$	$ 127,668
Total intangibles, net			$ 384,933			$ 287,011			$ 262,829

Intangible asset amortization expense for the three months ended March 31, 2007 and April 1, 2006 was approximately $3.7 million and $3.2 million, respectively. The estimated future amortization expense for identifiable intangible assets during the remainder of 2007 and the next five years is as follows:

In thousands	**2007 Q2 - Q4**	**2008**	**2009**	**2010**	**2011**	**2012**
Estimated amortization expense	$ 12,301	$ 15,417	$ 15,172	$ 14,660	$ 14,451	$ 13,538

10. Debt

Debt and the average interest rate on debt outstanding are summarized as follows:

In thousands	**Average interest rate**	**Maturity (Year)**	**March 31 2007**	**December 31 2006**	**April 1 2006**

	March 31, 2007				
Commercial paper, maturing within 54 days	5.75%		$ 243,267	$208,882	$166,261
Revolving credit facilities	5.78%	2010	325,673	25,000	230,600
Private placement fixed rate	5.50%	2007 - 2013	135,000	135,000	135,000
Private placement floating rate	5.96%	2013	100,000	100,000	100,000
Senior notes	7.85%	2009	250,000	250,000	250,000
Other	4.17%	2007 - 2016	23,900	21,972	6,318
Total contractual debt obligations			1,077,840	740,854	888,179
Interest rate swap monetization deferred income			2,915	3,207	4,082
Total debt, including current portion per balance sheet			1,080,755	744,061	892,261
Less: Current maturities			(8,257)	(7,625)	(4,246)
Short-term borrowings			(16,003)	(14,563)	
Long-term debt			$1,056,495	$721,873	$888,015

We have a multi-currency revolving Credit Facility (the Credit Facility) of $800 million expiring on March 4, 2010. The interest rate on the loans under the Credit Facility is LIBOR plus 0.625%. Interest rates and fees on the Credit Facility vary based on our credit ratings.

We are authorized to sell short-term commercial paper notes to the extent availability exists under the Credit Facility. We use the Credit Facility as back-up liquidity to support 100% of commercial paper outstanding. As of March 31, 2007, we had $243.3 million of commercial paper outstanding that matures within 54 days. All of the commercial paper was classified as long-term as we have the intent and the ability to refinance such obligations on a long-term basis under the Credit Facility.

Table of Contents

Pentair, Inc. and subsidiaries
Notes to condensed consolidated financial statements (unaudited)

We were in compliance with all debt covenants as of March 31, 2007.

We have $35 million of outstanding private placement debt maturing in May 2007. We classified this debt as long-term as of March 31, 2007 as we have the intent and ability to refinance such obligation on a long-term basis under the Credit Facility.

In addition to the Credit Facility, we have $25 million of uncommitted credit facilities, under which we had $16.0 million outstanding as of March 31, 2007.

Debt outstanding at March 31, 2007 matures on a calendar year basis as follows:

In thousands	**2007 Q2-Q4**	**2008**	**2009**	**2010**	**2011**	**2012**	**Thereafter**	**Total**
Contractual debt obligation maturities	$22,050	$1,290	$250,255	$604,135	$75	$6	$200,029	$1,077,840
Other maturities	874	1,166	875					2,915
Total maturities	$22,924	$2,456	$251,130	$604,135	$75	$6	$200,029	$1,080,755

11. Derivatives and Financial Instruments

Cash-flow hedges

In September 2005, we entered into a $100 million interest rate swap agreement with several major financial institutions to exchange variable rate interest payment obligations for fixed rate obligations without the exchange of the underlying principle amounts in order to manage interest rate exposures. The effective date of the fixed rate swap was April 25, 2006. The swap agreement has a fixed interest rate of 4.68% and expires in July 2013. The fixed interest rate of 4.68% plus the .60% interest rate spread over LIBOR, results in an effective fixed interest rate of 5.28%. The fair value of the swap was an asset of $1.4 million at March 31, 2007 and is recorded in *Other assets*.

The variable to fixed interest rate swap is designated as and is effective as a cash-flow hedge. The fair value of this swap is recorded on the Condensed Consolidated Balance Sheets, with changes in fair value included in other comprehensive income (OCI). Derivative gains and losses included in OCI are reclassified into earnings at the time the related interest expense is recognized or the settlement of the related commitment occurs.

In anticipation of issuing new debt in the second quarter of 2007 and to partially hedge the risk of future increases to the treasury rate, we entered into an agreement on March 30, 2007 to lock in existing ten-year rates on $200 million. The treasury rate was fixed at 4.64% and the agreement was settled on May 3, 2007.

The treasury rate lock agreement was designated as and was effective as a cash-flow hedge. The treasury rate lock agreement was settled at an interest rate of 4.67% and the corresponding settlement benefit of $0.5 million will be included in OCI in our Condensed Consolidated Balance Sheets, and will be recognized in earnings over the life of the debt after issuance. The agreement had no value at March 31, 2007.

12. Income Taxes

The provision for income taxes consists of provisions for federal, state and foreign income taxes. We operate in an international environment with operations in various locations outside the U.S. Accordingly, the consolidated income tax rate is a composite rate reflecting the earnings in the various locations and the applicable rates.

The effective income tax rate for the three months ended March 31, 2007 was 35.2% compared to 34.0% for the three months ended April 1, 2006. The first quarter 2006 effective tax included a $0.9 million favorable adjustment related to a prior year tax return. We expect the effective tax rate for the remainder of 2007 to be between 35.0% and 35.5%, resulting in a full year effective income tax rate of between 35.0% and 35.5%. However, we continue to actively pursue initiatives to reduce our effective tax rate. The tax rate in any quarter can be affected positively or negatively by adjustments that are required to be reported in the specific quarter of resolution.

We adopted the provisions of FIN 48 on January 1, 2007. As a result of the implementation of FIN 48, we recorded an adjustment to decrease retained earnings by $2.9 million.

Subsequent to the adjustment to retained earnings of $2.9 million, our total liability for unrecognized tax benefits as of January 1, 2007, the date of adoption, was $15.0 million, which if recognized, would affect our effective tax rate. Included in the total liability for unrecognized tax benefits of $15.0 million at the date of adoption was $1.8 million related to discontinued operations, which, if recognized, would affect the effective tax rate for discontinued operations.

We record penalties and interest related to unrecognized tax benefits in *Provision for income taxes* and *Net interest expense*, respectively, which is consistent with our past practices. As of January 1, 2007, we had recorded approximately $.3 million for the possible payment of penalties and $1.5 million related to the possible payment of interest.

Table of Contents

Pentair, Inc. and subsidiaries
Notes to condensed consolidated financial statements (unaudited)

We or one of our subsidiaries files income tax returns in the United States (U.S.) federal jurisdiction, various U.S. state jurisdictions and foreign jurisdictions. With few exceptions, we are no longer subject to U.S. federal, state and local, or foreign income tax examinations by tax authorities for years prior to 2002. The Internal Revenue Service (IRS) has audited us through 2003, and has completed a tax return survey of our 2004 federal income tax return. During the first quarter of 2007, our total liability for unrecognized tax benefits did not materially increase or decrease. It is reasonably possible that this gross liability for unrecognized tax benefits will decrease by $2.0 million during the next twelve months as a result of audits and the expiration of statutes of limitations in various jurisdictions.

13. Benefit Plans

Components of net periodic benefit cost for the three months ended March 31, 2007 and April 1, 2006 were as follows:

	Three months ended			
	Pension benefits		**Post-retirement**	
In thousands	**March 31 2007**	**April 1 2006**	**March 31 2007**	**April 1 2006**
Service cost	$ 4,331	$ 4,512	$ 146	$ 184
Interest cost	7,891	7,343	746	799
Expected return on plan assets	(7,133)	(6,974)		
Amortization of transition obligation	35	31		
Amortization of prior year service cost (benefit)	40	77	(62)	(59)
Recognized net actuarial loss	799	1,009	(355)	(212)
Net periodic benefit cost	$ 5,963	$ 5,998	$ 475	$ 712

14. Business Segments

Financial information by reportable segment for the three months ended March 31, 2007 and April 1, 2006 is shown below:

	Three months ended	
In thousands	**March 31 2007**	**April 1 2006**
Net sales to external customers		
Water	$555,412	$517,169
Technical Products	252,583	254,220
Consolidated	$807,995	$771,389
Intersegment sales		
Water	$ 214	$ 50
Technical Products	896	889
Other	(1,110)	(939)
Consolidated	$	$
Operating income (loss)		

Water	$ 60,879	$ 55,587
Technical Products	31,631	37,704
Other	(12,357)	(14,735)
Consolidated	$ 80,153	$ 78,556

Other operating loss is primarily composed of unallocated corporate expenses, costs related to our captive insurance subsidiary and our intermediate finance companies, and intercompany eliminations.

Table of Contents

Pentair, Inc. and subsidiaries
Notes to condensed consolidated financial statements (unaudited)

15. Warranty

The changes in the carrying amount of service and product warranties for the three months ended March 31, 2007 and April 1, 2006 were as follows:

In thousands	March 31 2007	April 1 2006
Balance at beginning of the year	$ 34,093	$ 33,551
Service and product warranty provision	12,233	9,415
Payments	(14,752)	(10,777)
Acquired	1,116	
Translation	76	49
Balance at end of the period	$ 32,766	$ 32,238

16. Commitments and Contingencies

Environmental and Litigation

There have been no further material developments from the disclosures contained in our 2006 Annual Report on Form 10-K.

Horizon Litigation

Twenty-eight separate lawsuits involving 29 primary plaintiffs, a class action, and claims for indemnity by Celebrity Cruise Lines, Inc. (Celebrity) were brought against Essef Corporation (Essef) and certain of its subsidiaries prior to our acquisition of Essef in August 1999. The claims against Essef and its involved subsidiaries were based upon the allegation that Essef designed, manufactured, and marketed two sand swimming pool filters that were installed as a part of the spa system on the Horizon cruise ship, and allegations that the spa and filters contained Legionnaire s disease bacteria that infected certain passengers on cruises from April 1994 through July 1994.

The individual and class claims by passengers were tried and resulted in an adverse jury verdict finding liability on the part of the Essef defendants (70%) and Celebrity and its sister company, Fantasia (together 30%). After expiration of post-trial appeals, we paid all outstanding punitive damage awards of $7.0 million in the Horizon cases, plus interest of approximately $1.6 million, in January 2004. All of the personal injury cases have now been resolved through either settlement or judgment.

The only remaining unresolved claims in this case were those brought by Celebrity for damages resulting from the outbreak. Celebrity filed an amended complaint seeking attorney fees and costs for prior litigation as well as out-of-pocket losses, lost profits, and loss of business enterprise value. On June 28, 2006, a jury returned a verdict against the Essef defendants in the total amount of $193.0 million for its claims for out-of-pocket expenses ($10.4 million), lost profits ($47.6 million) and lost enterprise value ($135.0 million). The verdict was exclusive of pre-judgment interest and attorneys fees.

On January 17, 2007, the Court ruled on our post-trial motions, granting judgment in our favor as a matter of law with respect to Celebrity s claim for lost enterprise value ($135.0 million). The Court also granted a new trial with respect to lost profits ($47.6 million). In addition, the Court denied without prejudice our claim for contribution to reduce Celebrity s recovery by 30% to account for its contributory negligence, with leave to renew the motion following retrial. The trial of this matter has been scheduled for June 2007.

Celebrity s claim for lost profits at trial amounted to approximately $60 million. We believe that actual lost profits suffered, if any, are substantially less. In a new trial, there remain questions of causation, contribution and proof of damages to be determined. We intend to vigorously defend against Celebrity s claims. We cannot predict whether Celebrity will appeal the ruling on lost enterprise value, nor whether and to what extent Essef may eventually be found liable on Celebrity s claims.

Several issues have not been decided by the Court, including whether Celebrity is entitled to recovery of its attorneys fees and related costs in the passenger claims phase of the case ($4.1 million), and, with respect to pre-judgment interest, the length of the interest period and the rate of interest on any eventual judgment. We have assessed the impact of the ruling on our previously established reserves for this matter and, based on information available at this time, have not changed our reserves following this ruling, except to take into account quarterly interest accruals.

We believe that any judgment we pay in this matter would be tax-deductible in the year paid or in subsequent years. In addition to the impact of any loss on this matter on our earnings per share when recognized, we may need to borrow funds from our banks or other sources to pay any judgment finally determined after exhaustion of all appeals. We expect that we would have available adequate funds to allow us to do so, based on discussions with our lending sources and our estimates of the results of our business operations over the foreseeable future.

Table of Contents

Pentair, Inc. and subsidiaries
Notes to condensed consolidated financial statements (unaudited)
17. Financial Statements of Subsidiary Guarantors

The $250 million Senior Notes due 2009 are jointly and severally guaranteed by domestic subsidiaries (the Guarantor Subsidiaries), each of which is directly or indirectly wholly-owned by Pentair (the Parent Company). The following supplemental financial information sets forth the condensed consolidated balance sheets as of March 31, 2007, December 31, 2006 and April 1, 2006, the related condensed consolidated statements of income for the three-months ended March 31, 2007 and April 1, 2006, and statements of cash flows for the three-months ended March 31, 2007 and April 1, 2006, for the Parent Company, the Guarantor Subsidiaries, the non-guarantor subsidiaries and total consolidated Pentair and subsidiaries.

Pentair, Inc. and Subsidiaries
Unaudited Condensed Consolidated Statements of Income
For the three months ended March 31, 2007

In thousands	**Parent Company**	**Guarantor Subsidiaries**	**Non-Guarantor Subsidiaries**	**Eliminations**	**Consolidated**
Net sales	$	$639,591	$ 212,432	$(44,028)	$807,995
Cost of goods sold		457,197	157,015	(43,620)	570,592
Gross profit		182,394	55,417	(408)	237,403
Selling, general and administrative	4,204	99,249	39,255	(408)	142,300
Research and development		11,507	3,443		14,950
Operating (loss) income	(4,204)	71,638	12,719		80,153
Net interest (income) expense	(14,044)	29,715	(551)		15,120
Income from continuing operations before income taxes	9,840	41,923	13,270		65,033
Provision for income taxes	3,416	15,009	4,478		22,903
Income from continuing operations	6,424	26,914	8,792		42,130
Gain on disposal of discontinued operations, net of tax	143				143
Net income	$ 6,567	$ 26,914	$ 8,792	$	$ 42,273

14

Table of Contents

Pentair, Inc. and subsidiaries
Notes to condensed consolidated financial statements (unaudited)

Pentair, Inc. and Subsidiaries
Unaudited Condensed Consolidated Balance Sheets
March 31, 2007

In thousands	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Assets					
Current assets					
Cash and cash equivalents	$ 6,980	$ 4,830	$ 52,420	$	$ 64,230
Accounts and notes receivable, net	174	405,288	173,584	(46,254)	532,792
Inventories		290,739	122,439		413,178
Deferred tax assets	97,313	34,212	6,232	(85,559)	52,198
Prepaid expenses and other current assets	16,047	12,571	28,845	(15,556)	41,907
Total current assets	120,514	747,640	383,520	(147,369)	1,104,305
Property, plant and equipment, net	4,500	208,644	138,067		351,211
Other assets					
Investments in subsidiaries	2,224,447	61,357	386,539	(2,672,343)	
Goodwill		1,469,309	361,050		1,830,359
Intangibles, net		258,108	126,825		384,933
Other	74,651	13,631	6,603	(25,380)	69,505
Total other assets	2,299,098	1,802,405	881,017	(2,697,723)	2,284,797
Total assets	$2,424,112	$2,758,689	$1,402,604	$(2,845,092)	$3,740,313
Liabilities and Shareholders Equity					
Current liabilities					
Short-term borrowings	$	$	$ 16,003	$	$ 16,003
Current maturities of long-term debt	1,167	257	284,178	(277,345)	8,257
Accounts payable	4,956	153,312	102,185	(51,740)	208,713
Employee compensation and benefits	9,942	39,559	36,240		85,741
Current pension and retirement medical benefits	7,918				7,918
Accrued product claims and warranties		27,225	15,541		42,766
Income taxes	327	8,628	4,570		13,525

Accrued rebates and sales incentives		25,898	5,395		31,293
Other current liabilities	22,516	48,764	29,456	(9,334)	91,402
Total current liabilities	46,826	303,643	493,568	(338,419)	505,618
Other liabilities					
Long-term debt	1,017,017	1,786,863	57,081	(1,804,466)	1,056,495
Pension and other retirement compensation	124,496	28,245	60,771		213,512
Post-retirement medical and other benefits	22,795	49,986		(25,380)	47,401
Long-term income taxes payable	14,412				14,412
Deferred tax liabilities	3,123	161,359	32,183	(85,559)	111,106
Due to / (from) affiliates	(540,814)	102,947	525,319	(87,452)	
Other non-current liabilities	30,400	7,157	48,355		85,912
Total liabilities	718,255	2,440,200	1,217,277	(2,341,276)	2,034,456
Shareholders equity	1,705,857	318,489	185,327	(503,816)	1,705,857
Total liabilities and shareholders equity	$2,424,112	$2,758,689	$1,402,604	$(2,845,092)	$3,740,313

Table of Contents

Pentair, Inc. and subsidiaries
Notes to condensed consolidated financial statements (unaudited)

Pentair, Inc. and Subsidiaries
Unaudited Condensed Consolidated Statements of Cash Flows
For the three months ended March 31, 2007

In thousands	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Operating activities					
Net income	$ 6,567	$ 26,914	$ 8,792	$	$ 42,273
Adjustments to reconcile net income to net cash provided by (used for) operating activities:					
Gain on disposal of discontinued operations	(143)				(143)
Depreciation	300	10,234	4,989		15,523
Amortization	931	2,942	1,027		4,900
Deferred income taxes	(498)		143		(355)
Stock compensation	6,218				6,218
Excess tax benefit from stock-based compensation	(1,063)				(1,063)
Intercompany dividends	(24)	24			
Changes in assets and liabilities, net of effects of business acquisitions and dispositions					
Accounts and notes receivable	11,062	(88,833)	(23,553)	1,937	(99,387)
Inventories		(7,051)	670		(6,381)
Prepaid expenses and other current assets	16,481	7,984	(26,213)	(7,022)	(8,770)
Accounts payable	(9,300)	(2,133)	21,290	(1,971)	7,886
Employee compensation and benefits	(5,312)	(8,943)	1,174		(13,081)
Accrued product claims and warranties		(1,729)	326		(1,403)
Income taxes	(1,806)	6,942	(6,584)		(1,448)
Other current liabilities	(10,134)	(12,625)	8,060	7,061	(7,638)
Pension and post-retirement benefits	2,468	681	884		4,033
Other assets and liabilities	(1,348)	1,412	1,103		1,167
Net cash provided by (used for) continuing operations	14,399	(64,181)	(7,892)	5	(57,669)
Net cash provided by (used for) operating activities of discontinued operations	(143)		143		
	14,256	(64,181)	(7,749)	5	(57,669)

Net cash provided by (used for) operating activities					
Investing activities					
Capital expenditures	(46)	(8,411)	(10,408)		(18,865)
Proceeds from sale of property and equipment		747	582		1,329
Acquisitions, net of cash acquired	(229,903)		(678)		(230,581)
Investment in subsidiaries	(98,247)	70,464	27,788	(5)	
Net cash (used for) provided by investing activities	(328,196)	62,800	17,284	(5)	(248,117)
Financing activities					
Net short-term borrowings (repayments)		(51)	1,285		1,234
Proceeds from long-term debt	345,190				345,190
Repayment of long-term debt	(10,250)				(10,250)
Proceeds from exercise of stock options	1,762				1,762
Repurchases of common stock	(9,280)				(9,280)
Excess tax benefits from stock-based compensation	1,063				1,063
Dividends paid	(15,022)				(15,022)
Net cash provided by financing activities	313,463	(51)	1,285		314,697
Effect of exchange rate changes on cash	(1,353)	(288)	2,140		499
Change in cash and cash equivalents	(1,830)	(1,720)	12,960		9,410
Cash and cash equivalents, beginning of period	8,810	6,550	39,460		54,820
Cash and cash equivalents, end of period	$ 6,980	$ 4,830	$ 52,420	$	$ 64,230

Table of Contents

Pentair, Inc. and subsidiaries
Notes to condensed consolidated financial statements (unaudited)

Pentair, Inc. and Subsidiaries
Unaudited Condensed Consolidated Statements of Income
For the three months ended April 1, 2006

In thousands	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Net sales	$	$633,060	$ 181,285	$(42,956)	$771,389
Cost of goods sold	125	459,223	132,073	(42,540)	548,881
Gross profit	(125)	173,837	49,212	(416)	222,508
Selling, general and administrative	6,221	93,541	29,743	(416)	129,089
Research and development		11,784	3,079		14,863
Operating (loss) income	(6,346)	68,512	16,390		78,556
Net interest (income) expense	(15,532)	29,786	(970)		13,284
Income from continuing operations before income taxes	9,186	38,726	17,360		65,272
Provision for income taxes	3,192	13,036	5,973		22,201
Income from continuing operations	5,994	25,690	11,387		43,071
Loss on disposal of discontinued operations, net of tax	(1,451)				(1,451)
Net income	$ 4,543	$ 25,690	$ 11,387	$	$ 41,620

17

Table of Contents

Pentair, Inc. and subsidiaries
Notes to condensed consolidated financial statements (unaudited)

Pentair, Inc. and Subsidiaries
Unaudited Condensed Consolidated Balance Sheets
April 1, 2006

In thousands	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Assets					
Current assets					
Cash and cash equivalents	$ 5,070	$ 5,276	$ 39,891	$	$ 50,237
Accounts and notes receivable, net	444	431,959	137,145	(48,580)	520,968
Inventories		284,297	91,322		375,619
Deferred tax assets	71,648	33,455	4,592	(65,263)	44,432
Prepaid expenses and other current assets	7,679	10,381	15,647	(4,786)	28,921
Total current assets	84,841	765,368	288,597	(118,629)	1,020,177
Property, plant and equipment, net	5,281	224,224	84,659		314,164
Other assets					
Investments in subsidiaries	1,982,627	43,937	90,489	(2,117,053)	
Goodwill		1,490,950	233,002		1,723,952
Intangibles, net		240,062	22,767		262,829
Other	55,077	6,517	5,967		67,561
Total other assets	2,037,704	1,781,466	352,225	(2,117,053)	2,054,342
Total assets	$2,127,826	$2,771,058	$725,481	$(2,235,682)	$3,388,683
Liabilities and Shareholders Equity					
Current liabilities					
Current maturities of long-term debt	$ 1,166	$ 231	$ 22,783	$ (19,934)	$ 4,246
Accounts payable	1,289	163,160	89,954	(47,875)	206,528
Employee compensation and benefits	9,203	39,137	27,196		75,536
Accrued product claims and warranties		27,398	14,840		42,238
Income taxes	8,594	7,496	11,105		27,195
Accrued rebates and sales incentives		21,558	1,795		23,353
Other current liabilities	21,902	54,829	22,450	(4,763)	94,418

Total current liabilities	42,154	313,809	190,123	(72,572)	473,514
Other liabilities					
Long-term debt	884,777	1,786,622	13,146	(1,796,530)	888,015
Pension and other retirement compensation	78,471	29,390	50,674		158,535
Post-retirement medical and other benefits	23,807	50,005			73,812
Deferred tax liabilities		162,860	26,066	(65,263)	123,663
Due to / (from) affiliates	(527,961)	205,621	242,104	80,236	
Other non-current liabilities	31,886	2,682	41,884		76,452
Total liabilities	533,134	2,550,989	563,997	(1,854,129)	1,793,991
Shareholders equity	1,594,692	220,069	161,484	(381,553)	1,594,692
Total liabilities and shareholders equity	$2,127,826	$2,771,058	$ 725,481	$(2,235,682)	$3,388,683

Table of Contents

Pentair, Inc. and subsidiaries
Notes to condensed consolidated financial statements (unaudited)

Pentair, Inc. and Subsidiaries
Unaudited Condensed Consolidated Statements of Cash Flows
For the three months ended April 1, 2006

In thousands	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Operating activities					
Net income	$ 4,543	$ 25,690	$ 11,387	$	$ 41,620
Adjustments to reconcile net income to net cash provided by (used for) operating activities:					
Loss on disposal of discontinued operations	1,451				1,451
Depreciation	400	11,299	3,531		15,230
Amortization	1,025	2,989	244		4,258
Deferred income taxes	3,024	(4,100)	3,559		2,483
Stock compensation	3,124	2,990	532		6,646
Excess tax benefit from stock-based compensation	(1,190)	(1,139)	(203)		(2,532)
Changes in assets and liabilities, net of effects of business acquisitions and dispositions					
Accounts and notes receivable	(370)	(93,520)	(16,198)	14,547	(95,541)
Inventories		(17,290)	(8,089)		(25,379)
Prepaid expenses and other current assets	10,546	(1,583)	(12,946)	(275)	(4,258)
Accounts payable	744	(6,669)	16,455	(14,571)	(4,041)
Employee compensation and benefits	(7,662)	(17,869)	2,003		(23,528)
Accrued product claims and warranties		(1,266)	(97)		(1,363)
Income taxes	(3,625)	15,934	(1,592)		10,717
Other current liabilities	(7,354)	(27,192)	8,107	299	(26,140)
Pension and post-retirement benefits	2,342	1,354	781		4,477
Other assets and liabilities	(3,407)	(676)	7,633		3,550
Net cash provided by (used for) continuing operations	3,591	(111,048)	15,107		(92,350)
Net cash provided by (used for) operating activities of discontinued operations	1,451		(1,403)		48
	5,042	(111,048)	13,704		(92,302)

Net cash provided by (used for) operating activities					
Investing activities					
Capital expenditures		(4,679)	(4,375)		(9,054)
Proceeds from sale of property and equipment		31	48		79
Acquisitions, net of cash acquired	(1,941)	(217)			(2,158)
Investment in subsidiaries	(109,439)	115,768	(6,329)		
Divestitures	(18,246)		(5,761)		(24,007)
Other	(1,750)	(400)			(2,150)
Net cash (used for) provided by investing activities	(131,376)	110,503	(16,417)		(37,290)
Financing activities					
Proceeds from long-term debt	272,906				272,906
Repayment of long-term debt	(133,051)				(133,051)
Proceeds from exercise of stock options	2,577				2,577
Excess tax benefits from stock-based compensation	1,190	1,139	203		2,532
Dividends paid	(14,224)				(14,224)
Net cash provided by financing activities	129,398	1,139	203		130,740
Effect of exchange rate changes on cash	(998)	320	1,267		589
Change in cash and cash equivalents	2,066	914	(1,243)		1,737
Cash and cash equivalents, beginning of period	3,004	4,362	41,134		48,500
Cash and cash equivalents, end of period	$ 5,070	$ 5,276	$ 39,891	$	$ 50,237

Table of Contents

Pentair, Inc. and subsidiaries
Notes to condensed consolidated financial statements (unaudited)

Pentair, Inc. and Subsidiaries
Unaudited Condensed Consolidated Balance Sheets
December 31, 2006

In thousands	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
ASSETS					
Current assets					
Cash and cash equivalents	$ 8,810	$ 6,550	$ 39,460	$	$ 54,820
Accounts and notes receivable, net	190	316,157	150,103	(44,316)	422,134
Inventories		283,687	115,170		398,857
Deferred tax assets	96,566	66,255	5,359	(117,602)	50,578
Prepaid expenses and other current assets	16,766	20,555	16,496	(22,578)	31,239
Total current assets	122,332	693,204	326,588	(184,496)	957,628
Property, plant and equipment, net	4,753	214,709	110,910		330,372
Other assets					
Investments in subsidiaries	1,978,466	61,351	134,204	(2,174,021)	
Goodwill		1,466,536	252,235		1,718,771
Intangibles, net		261,050	25,961		287,011
Other	76,076	15,078	5,423	(25,380)	71,197
Total other assets	2,054,542	1,804,015	417,823	(2,199,401)	2,076,979
Total assets	$2,181,627	$2,711,928	$855,321	$(2,383,897)	$3,364,979
LIABILITIES AND SHAREHOLDERS EQUITY					
Current liabilities					
Short-term borrowings	$	$	$ 14,563	$	$ 14,563
Current maturities of long-term debt	1,167	258	34,649	(28,449)	7,625
Accounts payable	3,053	158,294	94,709	(49,770)	206,286
Employee compensation and benefits	12,388	48,447	28,047		88,882
Current pension and post-retirement benefits	7,918				7,918
Accrued product claims and warranties		28,955	15,138		44,093
Income taxes	48,462	1,685	4,389	(32,043)	22,493

Accrued rebates and sales incentives		35,185	4,234		39,419
Other current liabilities	16,408	51,858	38,132	(16,395)	90,003
Total current liabilities	89,396	324,682	233,861	(126,657)	521,282
Other liabilities					
Long-term debt	695,924	1,786,914	40,987	(1,801,952)	721,873
Pension and other retirement compensation	121,680	27,470	58,526		207,676
Post-retirement medical and other benefits	23,143	50,079		(25,380)	47,842
Deferred tax liabilities	3,200	161,360	30,780	(85,559)	109,781
Due to / (from) affiliates	(453,623)	65,884	270,531	117,208	
Other non-current liabilities	31,908	7,322	47,296		86,526
Total liabilities	511,628	2,423,711	681,981	(1,922,340)	1,694,980
Shareholders equity	1,669,999	288,217	173,340	(461,557)	1,669,999
Total liabilities and shareholders equity	$2,181,627	$2,711,928	$855,321	$(2,383,897)	$3,364,979

Table of Contents

Pentair, Inc. and subsidiaries
Notes to condensed consolidated financial statements (unaudited)

18. Subsequent Event

On April 9, 2007, we entered into a $250 million 364-day Term Loan Agreement (the Facility) with Bank of America, N.A., and JPMorgan Chase Bank, N.A. Each lender has made $125 million available to us under the Facility. On April 30, 2007, we used $225.0 million of borrowings under the Facility to pay the cash purchase price of the Porous Media acquisition and the balance of the funds under the Facility were drawn for other corporate purposes. We announced the Porous Media acquisition on March 6, 2007.

On April 30, 2007, we acquired as part of our Water Group all of the capital interests in Porous Media, a privately held filtration and separation technologies business, for $225.0 million, excluding transaction costs and subject to a post-closing net asset value adjustment. Porous Media s product portfolio includes high-performance filter media, membranes and related filtration products and purification systems for liquids, gases and solids for general industrial, petrochemical, refining and healthcare market segments among others.

On May 3, 2007, we settled a treasury rate lock agreement that we entered into on March 30, 2007 to lock in existing ten-year rates on $200 million of anticipated new debt. Under this agreement, the treasury rate on such debt was fixed at 4.64%. The agreement was settled at an interest rate of 4.67% and the corresponding settlement benefit of $0.5 million will be included in OCI in our Condensed Consolidated Balance Sheets, and will be recognized in earnings over the life of the debt after issuance.

Table of Contents

ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

FORWARD-LOOKING STATEMENTS

This report contains statements that we believe to be forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements give our current expectations or forecasts of future events. Forward-looking statements generally can be identified by the use of forward-looking terminology such as may, will, expect, intend, estimate, anticipate, believe, project, or continue, or the negative thereo From time to time, we also may provide oral or written forward-looking statements in other materials we release to the public. Any or all of our forward-looking statements in this report and in any public statements we make could be materially different from actual results. They can be affected by assumptions we might make or by known or unknown risks or uncertainties. Consequently, we cannot guarantee any forward-looking statements. Investors are cautioned not to place undue reliance on any forward-looking statements. Investors should also understand that it is not possible to predict or identify all such factors and should not consider the following list to be a complete statement of all potential risks and uncertainties.

The following factors and those discussed in ITEM 1A, Risk Factors, included in our 2006 Annual Report on Form 10-K may impact the achievement of forward-looking statements:

changes in general economic and industry conditions, such as:

§ the strength of product demand and the markets we serve;

§ the intensity of competition, including that from foreign competitors;

§ pricing pressures;

§ market acceptance of new product introductions and enhancements;

§ the introduction of new products and enhancements by competitors;

§ our ability to maintain and expand relationships with large customers;

§ our ability to source raw material commodities from our suppliers without interruption and at reasonable prices;

§ our ability to source components from third parties, in particular from foreign manufacturers, without interruption and at reasonable prices; and

§ the financial condition of our customers;

our ability to successfully limit damages arising out of the Horizon litigation;

our ability to identify, complete, and integrate acquisitions successfully and to realize expected synergies on our anticipated timetable;

changes in our business strategies, including acquisition, divestiture, and restructuring activities;

domestic and foreign governmental and regulatory policies;

general economic and political conditions, such as political instability, the rate of economic growth in our principal geographic or product markets, or fluctuations in exchange rates;

changes in operating factors, such as continued improvement in manufacturing activities and the achievement of related efficiencies, cost reductions, and inventory risks due to shifts in market demand and costs associated with moving production overseas;

our ability to generate savings from our excellence in operations initiatives consisting of lean enterprise, supply management and cash flow practices;

unanticipated developments that could occur with respect to contingencies such as litigation, intellectual property matters, product liability exposures and environmental matters;

- our ability to accurately evaluate the effects of contingent liabilities such as tax, product liability, environmental, and other claims; and
- our ability to access capital markets and obtain anticipated financing under favorable terms.

The foregoing factors are not exhaustive, and new factors may emerge or changes to the foregoing factors may occur that would impact our business. We assume no obligation, and disclaim any duty, to update the forward-looking statements in this report.

Overview

We are a focused diversified industrial manufacturing company comprised of two operating segments: Water and Technical Products. Our Water Group is a global leader in providing innovative products and systems used worldwide in the movement, storage, treatment, and enjoyment of water. Our Technical Products Group is a leader in the global enclosures and thermal management markets, designing and manufacturing standard, modified, and custom enclosures that house and protect sensitive electronics and electrical components; thermal management products; and accessories. In 2007, we expect our Water Group and Technical Products Group to generate approximately 70% and 30% of total revenues, respectively.

Our Water Group has progressively become a more important part of our business portfolio with sales increasing from approximately $125 million in 1995 to approximately $2.2 billion in 2006. We believe the water industry is structurally attractive as a result of a growing demand for clean water and the large global market size (of which we have identified a target market totaling $60 billion). Our vision is to be a leading global provider of innovative products and systems used in the movement, storage, treatment, and enjoyment of water.

Our Technical Products Group operates in a large global market with significant potential for growth in industry segments such as defense, security, medical, and networking. We believe we have the largest enclosures industrial and commercial distribution network in North America and the highest enclosures brand recognition in the industry in North America. From mid-2001 through 2003, the Technical Products Group experienced significantly lower sales volumes as a result of severely reduced capital spending in the industrial and

Table of Contents

commercial markets and over-capacity and weak demand in the datacommunication and telecommunication markets. From 2004 through 2006, sales volumes increased due to the addition of new distributors, new products, and higher demand in targeted markets.

Key Trends and Uncertainties

The following trends and uncertainties affected our financial performance in the first three months of 2007 and will likely impact our results in the future:

- The housing market and new pool starts slowed dramatically in the first quarter of 2007 and also shrank in the last three quarters of 2006. We believe that construction of new homes and new pools starts in North America affects approximately 25% of the sales of our Water Group, especially for our pool and spa businesses. This downturn will likely have an adverse impact on our revenues for the remainder of 2007.
- The telecommunication equipment market, particularly in North America, has slowed over the past three quarters and impacted our North American electronics sales within our Technical Products Group. In the first quarter of 2007, North American electronics sales declined approximately 25% from the year earlier period. The revenue decrease is attributable to telecommunication industry consolidation (which has delayed enclosure product sales) and some datacommunication OEM programs reaching end-of-life. This weakness is anticipated to continue into our second quarter.
- We experience seasonal demand in a number of markets within our Water Group. End-user demand for pool equipment follows warm weather trends and is at seasonal highs from April to August. The magnitude of the sales spike is partially mitigated by employing some advance sales early buy programs (generally including extended payment terms and/or additional discounts). Demand for residential and agricultural water systems is also impacted by economic conditions and weather patterns, particularly by heavy flooding and droughts.
- We expect our operations to continue to benefit from our PIMS initiatives, which include strategy deployment; lean enterprise with special focus on sourcing and supply management, cash flow management, and lean operations; and IGNITE, our process to drive organic growth.
- We are experiencing material cost and other inflation in a number of our businesses. We are striving for greater productivity improvements and implementing selective increases in selling prices to help mitigate cost increases in base materials such as stainless steel and carbon steel and other costs such as health care and other employee benefit costs.
- We have a long-term goal to consistently generate free cash flow that equals or exceeds 100% conversion of our net income. Free cash flow, which we define as cash flow from operating activities less capital expenditures plus proceeds from sale of property and equipment, exceeded $200 million for the fourth consecutive year in 2005 and was $181 million in 2006. See our discussion of *Other financial measures* under the caption Liquidity and Capital Resources of this report.
- We experienced favorable foreign currency effects on net sales in the first three months of 2007. Our currency effect is primarily for the U.S. dollar against the euro, which may or may not trend favorably in the future.
- The effective tax rate for the first three months of 2007 was 35.2%. We estimate our effective income tax rate for the remainder of 2007 to be between 35.0% and 35.5%, resulting in a full year effective income tax rate of between 35.0% and 35.5%. We continue to actively pursue initiatives to reduce our effective tax rate. The tax rate in any quarter can be affected positively or negatively by adjustments that are required to be reported in the specific quarter of resolution.

Outlook

In 2007, our operating objective is to increase our return on invested capital by:

- Continuing to drive operating excellence through lean enterprise initiatives, with special focus on sourcing and supply management, cash flow management, and lean operations;
- Continuing the integration of acquisitions and realizing identified synergistic opportunities;
- Continuing proactive talent development, particularly in international management and other key functional areas;
- Achieving organic sales growth (in excess of market growth rates), particularly in international markets; and
- Continuing to make strategic acquisitions to grow and expand our existing platforms in our Water and Technical Products Groups.

The ability to achieve our operating objectives will depend, to a certain extent, on factors outside our control. See Forward-looking statements in this report and Risk Factors under ITEM 1A in our 2006 Annual Report on Form 10-K.

Table of Contents

RESULTS OF OPERATIONS

Net sales

Consolidated net sales and the change from the prior year period were as follows:

	Three months ended			
	March 31	**April 1**		**%**
In thousands	**2007**	**2006**	**$ change**	**change**
Net sales	$807,995	$771,389	$36,606	4.7%

The components of the net sales change in 2007 from 2006 were as follows:

Percentages	**% Change from 2006 First quarter**
Volume	0.9
Price	2.3
Currency	1.5
Total	4.7

Consolidated net sales

The 4.7 percent increase in consolidated net sales in the first quarter of 2007 from 2006 was primarily driven by:

- an increase in sales volume due to our February 2, 2007 acquisition of Jung Pumpen GmbH (Jung); and
- organic sales growth of approximately 2 percent (excluding acquisitions and foreign currency exchange), which included selective increases in selling prices to mitigate inflationary cost increases:
  - § higher sales of North American pool equipment due to shipments of fourth quarter 2006 early-buy program orders;

  This increase was partially offset by:
  - § lower Technical Products sales into electronics markets driven by mergers in the telecommunication equipment industry which have delayed buying activity and by datacommunication projects reaching end-of-life; and
  - § lower sales of pump and filtration products related to the downturn in the North American residential housing market; and
- favorable foreign currency effects.

Net sales by segment and the change from the prior year period were as follows:

	Three months ended			
	March 31	**April 1**		**%**
In thousands	**2007**	**2006**	**$ change**	**change**
Water	$555,412	$517,169	$38,243	7.4%
Technical Products	252,583	254,220	(1,637)	(0.6%)
Total	$807,995	$771,389	$36,606	4.7%

Water

The 7.4 percent increase in Water Group net sales in the first quarter of 2007 from 2006 was primarily driven by:

organic sales growth of approximately 4 percent (excluding acquisitions and foreign currency exchange), which included selective increases in selling prices to mitigate inflationary cost increases:

- § an increase in sales of North American pool equipment driven by new products and a carryover of fourth quarter 2006 early-buy program orders into the first quarter;

- § continued growth in China and in other emerging markets in Asia-Pacific as well as continued success in penetrating markets in Europe and the Middle East;

Table of Contents

These increases were partially offset by:

- § lower sales of pump and filtration products related to the downturn in the North American residential housing market;

an increase in sales volume driven by our February 2, 2007 acquisition of Jung; and

favorable foreign currency effects.

Technical Products

The 0.6 percent decrease in Technical Product Group net sales in the first quarter 2007 from 2006 was primarily driven by:

lower sales into electronics markets driven by mergers in the telecommunication equipment industry which have delayed buying activity and by datacommunication projects reaching end-of-life.

These decreases were partially offset by:

an increase in sales into electrical markets, which includes selective increases in selling prices to mitigate inflationary cost increases;

a strong sales performance in Asia driven by continued penetration in China; and

favorable foreign currency effects.

Gross profit

	Three months ended			
In thousands	**March 31 2007**	**% of sales**	**April 1 2006**	**% of sales**
Gross profit	$237,403	29.4%	$222,508	28.8%
Percentage Point Change		0.6pts		

The 0.6 percent increase in gross profit as a percentage of sales in the first quarter of 2007 from 2006 was primarily the result of:

selective increases in selling prices in our Water and Technical Products Groups to mitigate inflationary cost increases; and

savings generated from our PIMS initiatives including lean and supply management practices.

These increases were partially offset by:

inflationary increases related to raw materials and labor; and

higher cost as a result of a fair market value inventory step-up related to the Jung acquisition.

Selling, general and administrative (SG&A)

	Three months ended			
In thousands	**March 31 2007**	**% of sales**	**April 1 2006**	**% of sales**
SG&A	$142,300	17.6%	$129,089	16.7%
Percentage Point Change		0.9pts		

The 0.9 percentage point increase in SG&A expense as a percentage of sales in the first quarter of 2007 from 2006 was primarily due to:

proportionately higher SG&A spending in the acquired Jung business;

exit costs related to a previously announced 2001 French facility closure;

higher selling and general expense to fund investments in future growth with emphasis on growth in the international markets, including personnel and business infrastructure investments; and

Table of Contents

an increase in amortization expense related to the intangible assets from the Jung acquisition.

Research and development (R&D)

In thousands	March 31 2007	% of sales	April 1 2006	% of sales
	Three months ended			
R&D	$14,950	1.9%	$14,863	1.9%
Percentage Point Change		0.0pts		

R&D expense as a percentage of sales in the first quarter of 2007 was consistent with the first quarter of 2006.

Operating income

Water

In thousands	March 31 2007	% of sales	April 1 2006	% of sales
	Three months ended			
Operating income	$60,879	11.0%	$55,587	10.8%
Percentage Point Change		0.2pts		

The 0.2 percentage point increase in Water Group operating income as a percentage of sales in the first quarter of 2007 from 2006 was primarily the result of:

selective increases in selling prices to mitigate inflationary cost increases; and

savings generated from our PIMS initiatives including lean and supply management practices.

These increases were partially offset by:

inflationary increases related to raw materials and labor; and

higher cost as a result of a fair market value inventory step-up related to the Jung acquisition.

Technical Products

In thousands	March 31 2007	% of sales	April 1 2006	% of sales
	Three months ended			
Operating income	$31,631	12.5%	$37,704	14.8%
Percentage Point Change		(2.3) pts		

The 2.3 percentage point decrease in Technical Products Group operating income as a percentage of sales in the first quarter of 2007 from 2006 was primarily the result of:

inflationary increases related to raw materials such as stainless steel and labor costs;

lower sales into electronics markets driven by mergers in the telecommunication equipment industry which have delayed buying activity and by datacommunication projects reaching end-of-life; and

exit costs related to a previously announced 2001 French facility closure.

These decreases were partially offset by:

selective increases in selling prices to mitigate inflationary cost increases; and

savings realized from the continued success of PIMS, including lean and supply management activities.

Table of Contents

Net interest expense

In thousands	March 31 2007	Three months ended April 1 2006	Difference	% change
Net interest expense	$15,120	$13,284	$1,836	13.8%

The 13.8 percentage point increase in interest expense in the first quarter of 2007 from 2006 was primarily the result of:

- an increase in outstanding debt primarily related to the Jung acquisition; and
- an increase in interest rates in the first quarter of 2007 compared to the same period in 2006.

Provision for income taxes from continuing operations

In thousands	Three months ended March 31 2007	April 1 2006
Income before income taxes	$65,033	$65,272
Provision for income taxes	22,903	22,201
Effective tax rate	35.2%	34.0%

The 1.2 percentage point increase in the effective tax rate in the first quarter of 2007 from 2006 was primarily the result of:

- a favorable adjustment in the first quarter of 2006 related to a prior year tax return.

We estimate our effective income tax rate for the remaining quarters of this year will be between 35.0% and 35.5% resulting in a full year effective income tax rate of between 35.0% and 35.5%.

LIQUIDITY AND CAPITAL RESOURCES

Cash requirements for working capital, capital expenditures, equity investments, acquisitions, debt repayments, share repurchases, and dividend payments are generally funded from cash generated from operations, availability under existing committed revolving credit facilities, and in certain instances, public and private debt and equity offerings. We experience seasonal cash flows primarily due to seasonal demand in a number of markets within our Water Group. End-user demand for pool equipment follows warm weather trends and is at seasonal highs from April to August. The magnitude of the sales spike is partially mitigated by employing some advance sales early buy programs (generally including extended payment terms and/or additional discounts). Demand for residential and agricultural water systems is also impacted by weather patterns, particularly by heavy flooding and droughts.

The following table presents selected working capital measurements calculated from our monthly operating results based on a 13-month moving average:

Days	March 31 2007	December 31 2006	April 1 2006
Days of sales in accounts receivable	54	54	55
Days inventory on hand	77	76	71
Days in accounts payable	56	56	56

Operating activities

Cash used for operating activities was $57.7 million in the first three months of 2007 compared with cash used for operating activities of $92.3 million in the prior year comparable period. The decrease in cash used for operating activities was due primarily to lower cash used for working capital in the first quarter of 2007 versus the same period of last year. In the future, we expect our working capital ratios to improve as we are able to capitalize on our PIMS initiatives.

Investing activities

Capital expenditures in the first three months of 2007 were $18.9 million compared with $9.1 million in the prior year period. We currently anticipate capital expenditures for fiscal 2007 will be approximately $70 to $80 million, primarily for capacity expansions in our low cost country manufacturing facilities, implementation of a unified business systems infrastructure in Europe, new product development, and general maintenance capital.

On February 2, 2007, we acquired as part of our Water Group all the outstanding shares of capital stock of Jung Pumpen GmbH (Jung) for $230.2 million, including a cash payment of $239.9 million and transaction costs of $0.7 million, less cash acquired of $10.4 million. The purchase price is subject to a post-closing net asset value adjustment. Jung is a leading German manufacturer of wastewater products for municipal and residential markets. Jung brings us its strong application engineering expertise and a complementary product offering, including a new line of water re-use products, submersible wastewater and drainage pumps, wastewater disposal units and tanks. Jung also brings to Pentair its well-established European presence, a state-of-the-art training facility in Germany, and sales offices in Germany, Austria, France, Hungary, Poland and Slovakia. Goodwill recorded as part of the initial purchase price allocation was $103.2 million, of which approximately $53 million is tax deductible. We continue to evaluate the purchase price allocation for the Jung acquisition, including intangible assets, contingent liabilities, and property, plant and equipment. We expect to revise the purchase price allocation as better information becomes available.
Divestiture activities during 2006 relate to the following: In January 2006, pursuant to the purchase agreement for the sale of our former Tools Group, we completed the repurchase of a manufacturing facility in Suzhou, China from The Black and Decker Corporation (BDK) for approximately $5.7 million. We recorded no gain or loss on the repurchase. In March 2006, we completed an outstanding net asset value arbitration with BDK relating to the purchase price for the sale of our former Tools Group. The decision by the arbitrator constituted a final resolution of all disputes between BDK and us regarding the net asset value. We paid the final net asset value purchase price adjustment pursuant to the purchase agreement of $16.1 million plus interest of $1.1 million in March 2006, resulting in an incremental pre-tax loss on disposal of discontinued operations of $3.4 million or $1.6 million net of tax. Also in March 2006, we exited a leased facility from our former Service Equipment business resulting in a net cash outflow of $2.2 million and an immaterial gain from disposition.

Financing activities

Net cash provided by financing activities was $314.7 million in the first three months of 2007 compared with $130.7 million provided by financing activities in the prior year period. The increase primarily relates to the additional borrowings to fund the Jung acquisition. Financing activities included draw downs and repayments on our revolving credit facilities to fund our operations in the normal course of business, payments of dividends, cash used to repurchase Company stock, cash received from stock option exercises, and tax benefits related to stock-based compensation.
We have a multi-currency revolving Credit Facility (the Credit Facility) of $800 million expiring on March 4, 2010. We are authorized to sell short-term commercial paper notes to the extent availability exists under the Credit Facility. We use the Credit Facility as back-up liquidity to support 100% of commercial paper outstanding. As of March 31, 2007, we had $243.3 million of commercial paper outstanding that matures within 54 days. All of the commercial paper was classified as long-term as we have the intent and the ability to refinance such obligations on a long-term basis under the Credit Facility.
We were in compliance with all debt covenants as of March 31, 2007.
In addition to the Credit Facility, we have $25 million of uncommitted credit facilities, under which we had $16.0 million outstanding as of March 31, 2007.
On April 9, 2007, we entered into a $250 million 364-day Term Loan Agreement (the Facility) with Bank of America, N.A., and JPMorgan Chase Bank, N.A. Each lender has made $125 million available to us under the Facility. On April 30, 2007, we used $225.0 million of borrowings under the Facility to pay the cash purchase price of the Porous Media acquisition and the balance of the funds under the Facility were drawn for other corporate purposes. We announced the Porous Media acquisition on March 6, 2007.
Our current credit ratings are as follows:

Rating Agency	Long-Term Debt Rating	Current Rating Outlook
Standard & Poor s	BBB	Negative
Moody s	Baa3	Stable

On March 7, 2007, Standard & Poor s Ratings Services revised its current rating outlook on us from stable to negative. At the same time, Standard & Poor s affirmed its long-term debt rating of BBB . Standard & Poor s stated that the outlook revision reflects the additional leverage and stress on credit metrics that will result from the announced acquisition of Porous Media. The negative outlook indicates the rating could be lowered if financial policies become more aggressive or if operating results are weaker than expected.

As of March 31, 2007, our capital structure consisted of $1,080.8 million in total indebtedness and $1,705.9 million in shareholders equity. The ratio of debt-to-total capital at March 31, 2007 was 38.8 percent, compared with 30.8 percent at December 31, 2006 and 35.9 percent at April 1, 2006. Our targeted debt-to-total capital ratio is approximately 40 percent. We will exceed this target ratio from time to time as needed for operational purposes and/or acquisitions.

In anticipation of issuing new debt in the second quarter of 2007 and to partially hedge the risk of future increases to the treasury rate, we entered into an agreement on March 30, 2007 to lock in existing ten-year rates on $200 million. The treasury rate was fixed at 4.64% and the agreement was settled on May 3, 2007.

Table of Contents

The treasury rate lock agreement was designated as and was effective as a cash-flow hedge. The treasury rate lock agreement was settled at an interest rate of 4.67% and the corresponding settlement benefit of $0.5 million will be included in OCI in our Condensed Consolidated Balance Sheets, and will be recognized in earnings over the life of the debt after issuance.

We expect to continue to have cash requirements to support working capital needs and capital expenditures, to pay interest and service debt, to pay dividends to shareholders, and to repurchase Company stock. In order to meet these cash requirements, we intend to use available cash and internally generated funds, and to borrow under our committed and uncommitted credit facilities.

Dividends paid in the first three months of 2007 were $15.0 million, or $0.15 per common share, compared with $14.2 million, or $0.14 per common share, in the prior year period. We have increased dividends every year for the last 31 years and expect to continue paying dividends on a quarterly basis.

During 2006, the Board of Directors authorized the repurchase of shares of our common stock up to a maximum dollar limit of $100 million. As of December 31, 2006, we had purchased 1,986,026 shares for $59.4 million pursuant to this authorization during 2006. In December 2006, the Board of Directors authorized the continuation of the repurchase program in 2007 with a maximum dollar limit of $40.6 million. This authorization expires on December 31, 2007. As of March 31, 2007, we had repurchased an additional 312,400 shares for $9.3 million pursuant to this plan and, accordingly, we have the authority to repurchase additional shares up to a maximum dollar limit of $31.4 million for the remainder of 2007.

There have been no material changes with respect to the contractual obligations, other than noted above, or off-balance sheet arrangements described in our 2006 Annual Report on Form 10-K.

Other financial measures

In addition to measuring our cash flow generation or usage based upon operating, investing, and financing classifications included in the Consolidated Statements of Cash Flows, we also measure our free cash flow and our conversion of net income. We have a long-term goal to consistently generate free cash flow that equals or exceeds 100% conversion of net income. Free cash flow and conversion of net income are non-GAAP financial measures that we use to assess our cash flow performance. We believe free cash flow and conversion of net income are important measures of operating performance because they provide us and our investors a measurement of cash generated from operations that is available to pay dividends and repay debt. In addition, free cash flow and conversion of net income are used as a criterion to measure and pay compensation-based incentives. Our measure of free cash flow and conversion of net income may not be comparable to similarly titled measures reported by other companies. The following table is a reconciliation of free cash flow and a calculation of the conversion of net income with cash flows from continuing and discontinued operating activities:

	Three months ended	
In thousands	**March 31 2007**	**April 1 2006**
Net cash used for operating activities	$(57,669)	$ (92,302)
Capital expenditures	(18,865)	(9,054)
Proceeds from sale of property and equipment	1,329	79
Free cash flow	(75,205)	(101,277)
Net income	42,273	41,620
Conversion of net income	(177.9%)	(243.3%)

In 2007, our objective is to generate free cash flow that equals or exceeds 100% conversion of net income.

NEW ACCOUNTING STANDARDS

See Note 1 (New Accounting Standards) of ITEM 1.

CRITICAL ACCOUNTING POLICIES

In our 2006 Annual Report on Form 10-K, we identified the critical accounting policies which affect our more significant estimates and assumptions used in preparing our consolidated financial statements. We have not changed these policies from those previously disclosed in our Annual Report.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There has been no material changes in our market risk during the quarter ended March 31, 2007. For additional information, refer to Item 7A of our 2006 Annual Report on Form 10-K.

Table of Contents

ITEM 4. CONTROLS AND PROCEDURES

(a) Evaluation of Disclosure Controls and Procedures

We maintain a system of disclosure controls and procedures designed to provide reasonable assurance as to the reliability of our published financial statements and other disclosures included in this report. Our management evaluated, with the participation of our Chief Executive Officer and our Chief Financial Officer, the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the quarter ended March 31, 2007 pursuant to Rule 13a-15(b) of the Securities Exchange Act of 1934 (the Exchange Act). Based upon their evaluation, our Chief Executive Officer and our Chief Financial Officer concluded that our disclosure controls and procedures were effective as of the end of the quarter ended March 31, 2007 to ensure that information required to be disclosed by us in the reports we file or submit under the Exchange Act is recorded, processed, summarized, and reported, within the time periods specified in the Securities and Exchange Commission s rules and forms, and to ensure that information required to be disclosed by us in the reports we file or submit under the Exchange Act is accumulated and communicated to our management, including our principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosures.

(b) Changes in Internal Controls

There was no change in our internal control over financial reporting that occurred during the quarter ended March 31, 2007 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

30

Table of Contents

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Shareholders of Pentair, Inc.

We have reviewed the accompanying condensed consolidated balance sheets of Pentair, Inc. and Subsidiaries (the Company) as of March 31, 2007 and April 1, 2006, and the related condensed consolidated statements of income and cash flows for the three month periods ended March 31, 2007 and April 1, 2006. These interim financial statements are the responsibility of the Company s management.

We conducted our reviews in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to such condensed consolidated interim financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

We have previously audited, in accordance with standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of the Company as of December 31, 2006, and the related consolidated statements of income, changes in shareholders equity, and cash flows for the year then ended (not presented herein); and in our report dated February 26, 2007, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of December 31, 2006 is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

DELOITTE & TOUCHE LLP
Minneapolis, Minnesota
May 4, 2007

Table of Contents

PART II OTHER INFORMATION

ITEM 1. Legal Proceedings

Environmental and Litigation

There have been no further material developments from the disclosures contained in our 2006 Annual Report on Form 10-K, other than those matters identified below.

Horizon Litigation

Twenty-eight separate lawsuits involving 29 primary plaintiffs, a class action, and claims for indemnity by Celebrity Cruise Lines, Inc. (Celebrity) were brought against Essef Corporation (Essef) and certain of its subsidiaries prior to our acquisition of Essef in August 1999. The claims against Essef and its involved subsidiaries were based upon the allegation that Essef designed, manufactured, and marketed two sand swimming pool filters that were installed as a part of the spa system on the Horizon cruise ship, and allegations that the spa and filters contained Legionnaire s disease bacteria that infected certain passengers on cruises from April 1994 through July 1994.

The individual and class claims by passengers were tried and resulted in an adverse jury verdict finding liability on the part of the Essef defendants (70%) and Celebrity and its sister company, Fantasia (together 30%). After expiration of post-trial appeals, we paid all outstanding punitive damage awards of $7.0 million in the Horizon cases, plus interest of approximately $1.6 million, in January 2004. All of the personal injury cases have now been resolved through either settlement or judgment.

The only remaining unresolved claims in this case were those brought by Celebrity for damages resulting from the outbreak. Celebrity filed an amended complaint seeking attorney fees and costs for prior litigation as well as out-of-pocket losses, lost profits, and loss of business enterprise value. On June 28, 2006, a jury returned a verdict against the Essef defendants in the total amount of $193.0 million for its claims for out-of-pocket expenses ($10.4 million), lost profits ($47.6 million) and lost enterprise value ($135.0 million). The verdict was exclusive of pre-judgment interest and attorneys fees.

On January 17, 2007, the Court ruled on our post-trial motions, granting judgment in our favor as a matter of law with respect to Celebrity s claim for lost enterprise value ($135.0 million). The Court also granted a new trial with respect to lost profits ($47.6 million). In addition, the Court denied without prejudice our claim for contribution to reduce Celebrity s recovery by 30% to account for its contributory negligence, with leave to renew the motion following retrial. The trial of this matter has been scheduled for June 2007.

Celebrity s claim for lost profits at trial amounted to approximately $60 million. We believe that actual lost profits suffered, if any, are substantially less. In a new trial, there remain questions of causation, contribution and proof of damages to be determined. We intend to vigorously defend against Celebrity s claims. We cannot predict whether Celebrity will appeal the ruling on lost enterprise value, nor whether and to what extent Essef may eventually be found liable on Celebrity s claims.

Several issues have not been decided by the Court, including whether Celebrity is entitled to recovery of its attorneys fees and related costs in the passenger claims phase of the case ($4.1 million), and, with respect to pre-judgment interest, the length of the interest period and the rate of interest on any eventual judgment. We have assessed the impact of the ruling on our previously established reserves for this matter and, based on information available at this time, have not changed our reserves following this ruling, except to take into account quarterly interest accruals.

We believe that any judgment we pay in this matter would be tax-deductible in the year paid or in subsequent years. In addition to the impact of any loss on this matter on our earnings per share when recognized, we may need to borrow funds from our banks or other sources to pay any judgment finally determined after exhaustion of all appeals. We expect that we would have available adequate funds to allow us to do so, based on discussions with our lending sources and our estimates of the results of our business operations over the foreseeable future.

ITEM 1A. Risk Factors

There have been no material changes from the risk factors previously disclosed in ITEM 1A. of our 2006 Annual Report on Form 10-K.

Table of Contents

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

The following table provides information with respect to purchases we made of our common stock during the first quarter of 2007:

Period	(a) Total Number of Shares Purchased	(b) Average Price Paid per Share	(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	(d) Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs
January 1 - January 27, 2007	87,740	$ 30.08		$ 40,640,979
January 28 - February 24, 2007	18,170	$ 30.78		$ 40,640,979
February 25 - March 31, 2007	335,898	$ 29.82	312,400	$ 31,361,482
Total	441,808		312,400	

(a) The purchases in this column include shares repurchased as part of our publicly announced programs and in addition, 87,740 shares for the period January 1 January 27, 2007, 18,170 shares for the period January 28 February 24, 2007, and 23,498 shares for the period February 25 March 31, 2007 deemed surrendered to us by participants in our Omnibus Stock Incentive Plan and the

Outside Directors Nonqualified Stock Option Plan (the Plans) to satisfy the exercise price or withholding of tax obligations related to the exercise of stock options and non-vested shares.

(b) The average price paid in this column includes shares repurchased as part of our publicly announced programs and shares deemed surrendered to us by participants in the Plans to satisfy the exercise price or withholding of tax obligations related to the exercise price of stock options and non-vested shares.

(c) The number of shares in this column represents the number of shares repurchased as part of publicly announced programs to repurchase up to $100 million of our common stock.

(d) During 2006, the Board of Directors authorized the repurchase of shares of our common stock up to a maximum dollar limit of $100 million. As of December 31, 2006, we had purchased 1,986,026 shares for $59.4 million pursuant to this authorization during 2006. In December 2006, the Board of Directors authorized the continuation of the repurchase program in 2007 with a maximum dollar limit of $40.6 million. This authorization expires on December 31, 2007. As of March 31, 2007, we had repurchased an additional 312,400 shares for $9.3 million pursuant to this plan. As of April 27, 2007, we had not repurchased any additional shares under this plan and, accordingly, we have the authority to repurchase additional shares up to a maximum dollar limit of $31.4 million for the remainder of 2007.

Table of Contents

ITEM 6. Exhibits

(a) **Exhibits**

3.1 Third Restated Articles of Incorporation as amended through May 3, 2007.

3.2 Fourth Amended and Superseding By-Laws as amended through May 3, 2007.

4.1 Form of Term Loan Agreement for $250 million among Pentair, Inc., Bank of America, N.A. and JPMorgan Chase Bank, N.A. dated April 9, 2007 (incorporated by reference to Exhibit 99.1 to Pentair s Current Report on Form 8-K dated April 9, 2007).

15 Letter Regarding Unaudited Interim Financial Information.

31.1 Certification of Chief Executive Officer Pursuant to Rule 13a-14(a) of the Exchange Act, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certification of Chief Financial Officer Pursuant to Rule 13a-14(a) of the Exchange Act, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification of Chief Executive Officer, Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 Certification of Chief Financial Officer, Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

Table of Contents

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, on May 4, 2007.

PENTAIR, INC.
Registrant

By /s/ John L. Stauch
John L. Stauch
Executive Vice President and Chief Financial Officer
(Chief Accounting Officer)

Exhibit Index to Form 10-Q for the Period Ended March 31, 2007

3.1 Third Restated Articles of Incorporation as amended through May 3, 2007.

3.2 Fourth Amended and Superseding By-Laws as amended through May 3, 2007.

4.1 Form of Term Loan Agreement for $250 million among Pentair, Inc., Bank of America, N.A. and JPMorgan Chase Bank, N.A. dated April 9, 2007 (incorporated by reference to Exhibit 99.1 to Pentair s Current Report on Form 8-K dated April 9, 2007).

15 Letter Regarding Unaudited Interim Financial Information

31.1 Certification of Chief Executive Officer Pursuant to Rule 13a-14(a) of the Exchange Act, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certification of Chief Financial Officer Pursuant to Rule 13a-14(a) of the Exchange Act, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification of Chief Executive Officer, Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 Certification of Chief Financial Officer, Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.